United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

No. 76-7356

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

B

P/S

IN RE: MASTER KEY ANTITRUST LITIGATION

EXXON CORPORATION, ESSO EASTERN, INC., EXXON PRODUCTION RESEARCH COMPANY, ESSO EXPLORATION, INC., ESSO INTER AMERICA, INC., JAMAICA, INC., GIBRALCO, INC., EXXON NUCLEAR COMPANY, INC., and EXXON RESEARCH & ENGINEERING COMPANY,

Appellants,

Consolidated Appeals from the United States District Court for the District of Connecticut

APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

PRELIMINARY STATEMENT

Appellants Exxon Corporation, *et al.* ("Objectors") submit this reply to the answering briefs of Appellees Plaintiffs' Liaison Counsel, defendant Emhart Corporation ("Emhart"), and defendant Ilco Corporation ("Ilco/Unican").[1] Because of space and time limitations,[2] Ob-

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[1] Unican Security Systems Ltd. is Ilco's parent.

[2] Objectors consented to an accelerated briefing schedule in response to Plaintiffs' Liaison Counsel's motion to expedite in anticipation that argument might be entertained by this Court during the first three days of September, 1976. However, although argument is now set for the week of September 13, 1976, at the Pre-Argument Conference held on August 24, 1976, Emhart refused to consent to extend the time for filing this reply one day, to August 31, 1976. Appellees' answering briefs were served on August 24, 1976.

jectors will address only the highlights of Appellees' arguments, but do not concede any contention raised by Appellees which cannot be specifically addressed herein.

Part I of this brief summarizes the Appellees' arguments which are answered in this reply.

Part II answers Appellees' arguments that Objectors should bear the burden of showing that the Emhart and Ilco settlement proposals were unfair to the class members, despite the clear legal precedent that in class actions, the proponents of a compromise bear the burden of demonstrating its fairness and adequacy with credible evidence upon which reviewable findings may be made.

Part III replies to Appellees' arguments made in support of the District Court's summary approval of the premature plan of allocation in the Emhart settlement agreement.

Part IV replies to Appellees' arguments in support of the District Court's summary approval of the Ilco settlement.

I. SUMMARY OF APPELLEES' ARGUMENTS

Appellees' arguments are either irrelevant to the simple issues raised by the arbitrary 80%-20% Emhart "formula" and Ilco/Unicorn's financial responsibility, or constitute concessions that they failed to meet their burden of establishing a record at the "fairness hearings" which would demonstrate the reasonableness and adequacy of their proposals. Further, by offering arguments not put forth below or addressed by the District Court, Appellees have admitted that the District Court abused its discretion in summarily approving the settlement proposals over valid objections and without the entry of appropriate findings based on credible record evidence.

All Appellees basically argue the same theme: Plaintiffs' Liaison Counsel entered into settlements on behalf of the

classes; the District Court, despite the absence of a supporting record, summarily approved; the law favors compromises, and therefore, this Court should summarily affirm, despite the absence of reviewable findings in which the District Court articulated the factors motivating its rulings. This echoes the tenor of the proceedings below, namely, that Rule 23 class actions may be conducted as if they were designed to foster the interest of the attorneys, rather than the class members they represent.

In attempting to divert attention from the merits, Appellees have disparaged Objectors' arguments because they are, concededly, only a few of the many class members, most of whom did not voice opposition below. However, class counsel do not encourage scrutiny, much less opposition, to their conduct of the litigation. This is fully evident from the limited and short notice of the Ilco "fairness hearing" which resulted from the following colloquy in chambers:

> MR. FREEMAN: . . . [G]iven the *inadequate* size of that settlement in relation to the potential liability and really the small amount of settlement it wouldn't be worth while to publish notice . So that puts an added burden on us, we feel, and probably the Court. (Emphasis supplied.)
>
> * * *
>
> THE COURT: Some notice has to be given. The rules require it.
>
> MR. MONTAGUE: Your Honor, may I just suggest . . . that I know of where a Court has said where there's a small defendant who settles, where it will not have any significant effect on the financial outcome of the case, no notice is necessary . . . (A623-A624).

In short, the cavalier manner in which Objectors' arguments are treated is typical of the *pro forma* fashion in which these settlement proceedings were handled below. This was further made clear, for example, by the provision

which reserved the proceeds of the Ilco settlement for the use of plaintiffs' counsel (A875-A876). The fact that Objectors have sought appellate review provides this Court with a unique opportunity to decide issues of fundamental importance in the administration of class action settlements. Both the Emhart settlement allocation provision and the Ilco settlement raise serious questions affecting the interests of class members.

II. THE BURDEN OF PROVING FAIRNESS AND ADEQUACY IS ON THE SPONSORS OF A SETTLEMENT PROPOSAL

All Appellees attempt to place on Objectors the burden of disproving the fairness of the Emhart allocation provision and the adequacy of the Ilco settlement, and thereby urge this Court to ignore the rule of law that the *proponents* of a class action settlement must demonstrate its adequacy and fairness. *United Founders Life Insurance Co.* v. *Consumers National Life Insurance Co.*, 447 F.2d 647, 652 (7th Cir. 1971); *Fricke* v. *Daylin*, 66 F.R.D. 90, 97 (E.D.N.Y. 1975); *Zerkle* v. *Cleveland-Cliffs Iron Co.*, 52 F.R.D. 151 (S.D.N.Y. 1971); *Norman* v. *McKee*, 290 F. Supp. 29 (N.D. Cal. 1968). At the May 21, 1976 conference in chambers, it was clear that counsel recognized that it was *their* burden to demonstrate the fairness of the settlements (A619-A620; A622). In fact, Plaintiffs' Liaison Counsel stated:

> MR. FREEMAN: . . . I think it is our obligation to assure the Court, on behalf of everybody, so that we are protecting the class members in this situation.
>
> THE COURT: All right.
>
> That's why I wanted some kind of an affidavit from you, or somebody else that this has been done, to satisfy the record (A630).

Nonetheless, neither Plaintiffs' Liaison Counsel nor Ilco provided the affidavits which they agreed to submit (A619; A622; A630). Emhart would likewise impose on Objectors,

the burden of demonstrating the unfairness of the 80%-20% "formula" (Emhart's Br. at 1, 22-26). However, the District Court held in approving the Emhart settlement that the very data which Emhart criticizes Objectors for not having offered was simply "not available at this time" (A839).

Although Appellees have been involved in this litigation for years—and thus have had full access to all discovery materials—they have not presented objective evidence from the discovery record in support of the settlement proposals. As to Emhart, Appellees had at least one full year to develop meaningful, objective support for the 80%-20% "formula". And as to Ilco, Appellees did not even support their application with the affidavits specifically requested by the Court one month earlier (A620; A630; A634-A636).

Objectors received notice of the settlements and "fairness hearings" only shortly in advance and these notices provided little substantive information. In fact, it takes time for concerned class members to become apprised of the issues involved in complex litigation and to evaluate the possible avenues of inquiry. The notices stated that class members could appear at "fairness hearings" at which the adequacy of the settlements would be demonstrated, although Appellees presented no credible support for their proposals. Brief, conclusory *affidavits of counsel* (or their staff) were the only offerings of the sponsors of either settlement.

This situation contrasts sharply with the factual showings made by proponents of other settlements. In *Blank* v. *Talley Industries, Inc.*, 64 F.R.D. 125, 127 (S.D.N.Y. 1974), the Court noted that many affidavits, exhibits and memoranda had been submitted in support of the settlement. In *Greenspun* v. *Bogan*, 492 F.2d 375, 378-379 (1974), the First Circuit remarked that the proponents of the settlement had filed depositions and two volumes of exhibits and documents in support of the settlement. Likewise, in

United Founders Life Insurance Co., supra, 447 F.2d at 657, the Seventh Circuit noted that the District Court had at its disposal *evidentiary* material supporting the proponents' position, and in *Grunin* v. *International House of Pancakes,* 513 F.2d 114, 125 (8th Cir. 1975), the Eighth Circuit catalogued the vast evidence of the defendant's financial condition which the District Court examined before approving the settlement.[3]

Here, the District Court relied *solely* on the assurances and affidavits of counsel in approving the settlements. This is improper when complex financial questions are involved, especially when counsel have expressly disavowed any financial expertise (A621; A971; A981). In *Levin* v. *Mississippi River Corp.,* 59 F.R.D. 353, 367 (S.D.N.Y. 1973), the District Court emphasized that it acted with the "advice of experienced independent railroad investment advisers and analysts." Similarly, in *Blank* v. *Talley Industries, supra,* the District Court relied on the fact that "investment analysts and advisers" had deemed the settlement fair. 64 F.R.D. at 132.

Thus, those sponsoring the Emhart plan of allocation and the Ilco settlement did not meet their burden. As stated by Professors Wright and Miller:

> [T]he standard used by the courts in evaluating a compromise is that the proposal must be fair and reasonable and in the best interests of *all those who will be affected by it. The burden is on the proponents of the settlement to show that it meets this standard.* The main judicial concern is that the rights of the passive class members not be jeopardized by the proposed action. The court also must be sensitive to the possibility of collusion between the parties actually participating in the action. Wright & Miller, 7A *Federal Practice and Procedure,* § 1797, at 229-230 (1972). (Footnotes omitted; emphasis supplied.)

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3 Counsel for the private-entities and public-bodies in this case was also involved in the *Grunin* litigation.

The absence of a supporting record is illustrated by the resulting inability of the District Court to make findings articulating the factors underlying its summary conclusions. This is all the more striking by comparing the Memorandum of Decision entered below with the recent decision by the same District Court cited in Emhart's Brief (at 42, note).[4] That twenty-two page decision is replete with references to the relevant facts, but such an opinion was not, and could not have been written on the records below of either the Emhart or Ilco "fairness hearings". Likewise, in its landmark decision in *Detroit* v. *Grinnell Corp.*, 495 F.2d 448, 468 (2nd Cir. 1974), this Court noted the thorough consideration given by the District Court in its decision approving that settlement which extensively set forth the relevant facts.

In short, the Court below has ignored the warning of this Court in *Saylor* v. *Lindsley*, 456 F.2d 896 (1972) as echoed by Judge Gurfein in *Weiss* v. *Chalker*, 55 F.R.D. 168, 169 (S.D.N.Y. 1972):

> [U]nless the District Court has available to it either hard facts or a rational explanation for inability to discover them, . . . it is flying blind.

This is precisely the case with respect to both the Emhart plan of allocation and the Ilco settlement.

III. THE EMHART PLAN OF ALLOCATION

Both Plaintiffs' Liaison Counsel and Emhart attempt to mischaracterize the issues on appeal. This appeal does *not* involve either (a) whether the District Court should have approved the amount of the Emhart settlement offer or (b) whether the District Court should have approved the 80%-20% plan of allocation *if* it had been based on Em-

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[4] *Herbst* v. *Int'l Tel. & Tel. Corp.*, Civil Action No. 15,155 (D. Conn. August 11 1976).

hart's contemporaneous records or other substantial evidence *and* if these records or other evidence were legally relevant. (Plaintiffs' Br. at 1, 26; Emhart's Br. at 13). Virtually without exception, the case law cited by Appellees treats broad questions which are not at issue here, namely the standards for approving the *amount* of a settlement, rather than the narrow allocation issue which is before this Court.

Further, despite Appellees' contentions, the arbitrary 80%-20% "formula" below was *not* supported by contemporaneous business records containing that allocation. The only documents presented at the "fairness hearing" relating to the purported "division" of Emhart's sales between public-body and private-entity classes were *summary tabulations prepared by Plaintiffs' Liaison Counsel and posited on arbitrary assumptions* about various categories of Emhart's sales.

A. The Settlement Amount Has Not Been Challenged

Appellees attempt to shift the focus away from the arbitrary plan of allocation to the settlement itself. Objectors have not questioned whether the $7.5 million settlement is within an acceptable range of fairness. Likewise, it is conceded that a trial court has broad latitude in passing on the adequacy and fairness of the *amount* of a settlement offer based on a variety of factors such as the complexity of the litigation, difficulty of proving liability, problems as to proof of damages, and the multiplicity of other unquantifiable factors dwelled on by Appellees.

But those factors which may be weighed in various ways when the amount of a settlement is being evaluated are wholly irrelevant when a specific plan of allocation is being reviewed as to its fairness to certain class members. Here, the starting point has already been quantified, *i.e.*, the $7.5 million settlement amount. *This amount has also already been judicially determined to be a fair settlement of the*

claims of all class members, and no issue on appeal has been raised as to the propriety of that approval. The public-bodies did not file a protective cross-appeal challenging the amount of the settlement in the event that the plan of allocation is stricken. *Again, Emhart has, in fact, settled this case for an amount which the District Court held was fair to all class members.*

Emhart now belatedly defends the plan of allocation, but, of course, its main concern has understandably been with the amount of the settlement. Emhart's extensive Memorandum filed below addressed virtually exclusively the amount of the settlement (A541-A570). At the "fairness hearing" Emhart's counsel did address exclusively the adequacy of the amount of its settlement offer (A686-A690). In this appeal, Emhart also relies primarily on cases addressing and factors relating to the fairness and adequacy of the *amount* of a class action settlement.

Both Emhart and Plaintiffs' Liaison Counsel now chart a direction wholly different from that which they presented to the District Court. At the June 2, 1976, "fairness hearing", counsel for Emhart candidly stated that Emhart would pay no more than $7.5 million for the disposition of *all* classes' claims (A687), regardless of how the proceeds would be distributed:

> When Lee Freeman and I reached this settlement about a year ago, we each believed, . . . that the figure of seven and a half million dollars . . . is . . . fair to *all the plaintiffs* . . . (A689). (Emphasis supplied.)

Emhart now argues vigorously that of the $7.5 million it agreed to pay, the public bodies had not demanded $6 million (Emhart's Br. at 6), but this is directly contradicted by the statement of Plaintiffs' Liaison Counsel:

> MR. FREEMAN: The settlement was accepted by the fourteen or fifteen states who have filed suit on the basis of the $6 million being paid to the public entities (A679).

Moreover, in addition to the statements in open court, in their Memorandum filed below in support of the Emhart settlement proposal, Plaintiffs' Liaison Counsel made the following concession as to the origin of the plan of allocation:

> There were several meetings and numerous discussions among plaintiffs' counsel prior to complete acceptance and filing of the settlement agreement . . . . *These discussions* [*among plaintiffs' counsel*] *led to agreement on . . . the allocation between the public and private classes* . . . (A527). (Emphasis supplied.)

In short, as a result of *negotiation* between plaintiffs' counsel, an agreement was reached whereby the public-bodies were guaranteed $6 million of the $7.5 million Emhart settlement fund. Emhart's disclaimer that the public-bodies did not demand $6 million is contradicted by the public-bodies themselves, whose adamant opposition to having the settlement proceeds fairly distributed to all class members under a claims procedure—without the premature $6 million guarantee—is the very reason that this appeal is pending!

In fact, although flying in the face of all practicalities now that (a) the settlement has proceeded this far, (b) the settlement amount has been approved by the District Court as fair to all classes, and (c) no cross appeal has been filed, Appellees suggest that the public bodies demand a $6 million guarantee by way of the plan of allocation or else they may withdraw from the settlement. If, in fact, the 80%-20% "formula" truly reflected the injury inflicted on all class members, there would be no need for the public-bodies to insist on the premature plan of allocation. Under a claims procedure, after all claims are filed based on the actual purchasing experience of each class member electing to participate in the settlement, the public-bodies would, in fact, receive at least 80% of the total settlement fund *if* they accounted for 80% or more percent of total purchases. Hence, the public-bodies' adamant opposition to a claims

procedure which would be eminently fair to *all* class members is a dispositive concession that they have no confidence that the 80%-20% "formula" or $6 million guarantee is grounded on sound data or truly representative of the portion of purchases actually accounted for by them.

Plaintiffs' Liaison Counsel contend that a claims procedure would be unduly burdensome and impede trial. These objections are patently frivolous. It is difficult to imagine that Plaintiffs' Liaison Counsel intend to make a distribution of the $7.5 million settlement proceeds now with the imminent prospect of the trial being completed or other settlements concluded with the two remaining non-settling defendants. *Any* distribution whether by a claims procedure or otherwise would impede trial preparation. Also, piece-meal distribution by varying formulae would merely increase the costs of administration unnecessarily and constitute imprudent management of the *classes'* settlement fund. Further, the claim of sudden urgency is difficult to fathom when the sponsors of the settlement waited from June 26, *1975,* when the settlement was reached, to June 2, *1976* to present the proposal to the Court.

This highlights another difficulty arising *solely* from basing the 80%-20% "formula" on the so-called "Emhart Data." Although there is some question as to what, in fact, has been done, at the hearing on the Ilco settlement, the District Court stated that the Ilco settlement proceeds are "going into the same fund and earn the same kind of interest that the escrow fund made up of Emhart's settlement is making" (A995). Moreover, this would also be true presumably as to any funds received from the other defendants. The costs of administration would obviously be increased and the mechanics of administration multiplied if the fund is to be allocated on the basis of four inconsistent formulae applied to amounts received from each of the defendants either after judgment or by way of settlement. The other alternative is even more disturbing, namely that the 80%-20% "formula", albeit arbitrary,

will serve as a model for agreements with the remaining two defendants, to the even greater detriment of the private-entity class.

Plaintiffs' Liaison Counsel suggest that distribution of any settlement funds to public-bodies might be on a demographic basis, while the private-entities would file claims, (Plaintiffs' Br. at 52). This merely highlights both the discriminatory fashion in which the private-entity class has been treated, and the conflict of interest of counsel representing two classes.

s' answer to Objectors' contention that there is a conflict of interest in this case is non-responsive. Emhart argues that there is only a *potential* conflict of interest and that Objectors have not "presented any suggestion that this potential conflict has in any way been detrimental to the private class" (Emhart's Br. at 33). To the contrary, throughout the proceeding below Objectors consistently urged that a plan of allocation agreed to by counsel representing two classes with antagonistic interests presented an existing, actual conflict of interest (A755; A818-A820; A852). This is now highlighted by the suggestion that the methods of distribution of the settlement fund to the two classes can be different. However, the burden of the cost of administration and distribution of the fund imposed on each class would not be the same, and would be discriminatory to private-entities.

Plaintiffs' Liaison Counsel make three responses to the conflict of interest noted by the District Court (A684; A839), but none of them is valid. The argument that there is no conflict of interest because both classes are end-users is totally irrelevant because *the very plan of allocation discriminates against the private-entities.* Also, the plan of allocation was formulated after the classes were certified, and the Court's prior decisions were rendered before this problem arose. Likewise, in the *Grinnell* case, there was *no arbitrary allocation among classes,* but rather the funds

were distributed under a claims procedure as is generally the case. Finally, the argument that the conflict did not affect the allocation of the settlement is specious because the claimed data which is given as support for the 80%-20% "formula" does not, in fact, support the allocation.

Plaintiffs rely on *West Virginia* v. *Chas. Pfizer & Co.*, 404 F.2d 1079 (2d Cir. 1971), for the proposition that this Court rejected a similar objection to a settlement allocation, but the very language quoted from that decision reveals that the conflict of interest was resolved on the basis of *affidavits,* which were not submitted below. The suggestion that the problem was remedied by the District Court's appointment of separate counsel to represent the private entities is also irrelevant. To the contrary, the District Court both at the "fairness hearing" (A684) and in its decision recognized the existing conflict of interest, and in response, took steps to remedy it *in futuro.* The Court's remedial action could not and did not retroactively remove the stigma from the Emhart settlement which will remain so long as the plan of allocation is part of the agreement.

Also, the suggestion that there is only an apparent or potential conflict of interest which can be ignored is both a dispositive concession, and contrary to the holdings of this Court as set forth by Chief Judge Kaufman in *General Motors Corp.* v. *New York*, 501 F.2d 639, 649 (1974), where the rationale for avoiding even the appearance of impropriety was fully expounded:

> Accordingly, without in the least even intimating that . . . he is guilty of any actual impropriety . . ., we must act with scrupulous care to avoid any *appearance* of impropriety lest it taint . . . the legal profession. (Emphasis by the Court.)

Finally, the arbitrary plan of allocation is not an integral part of and is severable from the Emhart settlement agreement. Any contrary contention would be prem-

ised on the assumption that the District Court was a "rubber stamp" which must approve, *in toto,* any settlement presented despite the fact that certain provisions of the settlement proposal may be unfair or contrary to sound public policy such as the clause reserving the Ilco settlement proceeds for counsel (A875-A876). This contention, if endorsed by this Court, would eviscerate the due process notice requirements of Rule 23(e). Accordingly, the District Court's own notice provided:

> The fairness and reasonableness of the amount of the settlement *and the allocation of the fund between the public entities and private builder-owner classes* is subject to the approval of the court (A400). (Emphasis supplied.)

Thus, the Court's notice specifically provided for evaluating the amount of the settlement separate and apart from the plan of allocation. In fact, the District Court itself questioned whether the 80%-20% "formula" was an "inviolate" provision of the settlement agreement, and Plaintiffs' Liaison Counsel replied only that it met the public bodies' demand for a guaranteed $6 million (A681).

B. The "Emhart Data"

Despite repeated assertions to the contrary, the so-called "Emhart Data" purportedly supporting the 80%-20% "formula" is *not,* in fact, taken from Emhart's contemporaneously generated business records. Emhart itself admits that the alleged support for the "formula" is at best "derived from" records of Emhart (A566). There is a critical difference between information taken directly from contemporaneous business records, such as total sales to all purchasers which could merely be arithmetically tallied, and a *breakdown* of sales to public-bodies versus private-entities which is *not* contained in the annual summaries of Emhart's sales submitted below (A594-A599).

Appellees repeatedly refer to "contemporaneous" business records as if the cloak of "contemporaneousness" makes a document suitable for all purposes regardless of its inherent limitations. The Emhart records are on their face inadequate to distinguish between sales to private-entities and public-bodies; only an analysis of the documents *underlying* the summary Dodge Project Construction Contract summaries would permit such a breakdown.[5]

Accordingly, Appellees' contention that Objectors have not opposed the amount of the settlement but only the allocation provision, even though both are purportedly grounded on the same records is non-responsive. It was necessary to go *beyond* the Emhart records themselves and to make arbitrary assumptions in order to support the 80%-20% "formula." The inadequacy of the Emhart records in question is best exemplified by a brief review of the Dodge summaries themselves which were submitted to the Court *for the first time* at the June 2, 1976, "fairness hearing" (A592-A593). The 80%-20% "formula" depends upon an *analysis* of the data, contained in the Dodge Construction Contract Order Forms as admitted in the Gibbs Affidavit (A592). This called for the exercise of independent judgment based on expertise in the trade. Presumably, Emhart has experienced personnel who might have made such an analysis, and all parties have retained experts (Emhart's Br. at 5; Plaintiffs' Br. at 6) who could perhaps have sponsored the exhibits. Instead, they were sponsored by an employee for counsel representing public-

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[5] Under Rule 1006 of the Federal Rules of Evidence, it is doubtful that the Dodge tabulations would be admissible unless Emhart produced the underlying data from which they are presumably derived. As commentators have noted, this Rule means that "charts, summaries or calculations are inadmissible . . . where the person responsible for the exhibit's preparation incorporates in the exhibit facts drawn from his personal knowledge . . . or statements made to him by knowledgeable persons" 5 Weinstein's *Evidence* ¶ 1006[03] (1975).

bodies, who could not even authenticate the documents. In fact, there is no suggestion that Emhart has ever authenticated them.

Despite repeated statements that discovery was extensive and the District Court was familiar with this case, no evidentiary material breaking down Emhart's sales to public-bodies versus private-entities was ever presented to the Court prior to this hearing. Moreover, it is respectfully submitted that there is nothing in the District Court's brief, conclusory Memorandum Of Decision which reflects that it ever reviewed the exhibits to the Gibbs' Affidavit, and thereby learned that the records attached thereto do not even mention the terms "public" or "private" buildings, nor do they contain any other delineation of data which can be interpreted as distinguishing between the public-body versus private-entity sectors. The conclusory statements in the memoranda filed below pertaining to the "Emhart Data" did not include those exhibits, and presumably, but for the objections filed to the plan of allocation, even the Gibbs' Affidavit would not have been submitted, and it was untimely filed several weeks after the May 13, 1976 deadline (A400). In fact, there is not even a description in the record of Ms. Gibbs' background, nor any claim of her expertise to make the so-called "analysis" which she undertook at the direction of her employer, Plaintiffs' Liaison Counsel (A592).

Presumably, Appellees fully expected the District Court to "rubber-stamp" their settlement proposal without the need for them to present any supporting evidence whatsoever. If the Gibbs' Affidavit had been timely filed, the District Court and Objectors could have reviewed the data presented prior to the "fairness hearing" and questioned the affiant. However, Ms. Gibbs was not called as a witness to explain her affidavit much less tendered for the acid test of cross-examination.

Further, the inadequacy of the Emhart records for determining a breakdown of sales to public-bodies versus private-entities is *now admitted by Emhart.* Emhart states that it "recognized" that the categories of "Education and Science" and "Dormitories" contain "some" private construction (Emhart's Br. at 15). Emhart then states that information *outside* of its records—obtained from the Department of Health, Education and Welfare—shows the portion of private school enrollment and suggests that the margin of error is not gross. The fact of the matter is that error of unknown magnitude has been introduced by the assignment of various categories of purchases entirely to the public sector.

Likewise, Emhart tries to support the data by saying that "the 80%-20% allocation also gave recognition to other factors which are less easily quantified" (Emhart's Br. at 15). It then contends that the alleged illegal overcharges might have been higher on extensions of master key systems and that there are more extensions in the public sector than in the private sector. Significantly, there is no record citation to support those contentions, and it merely shows the *arbitrariness* of the support for the 80%-20% "formula" which the Court apparently thought did in fact delineate between public-bodies and private-entities (A685).

It is simply incredible that despite their fiduciary duties, counsel would attempt to reserve $6 million for their clients on the basis of a summary affidavit of an employee. The judicial concern with the pitfalls of attorneys becoming witnesses for their clients was noted by the District Court at the conference held in chambers on May 21, 1976 (A621). Also, in *Weiss* v. *Chalker,* 55 F.R.D. 168, 171 (S.D. N.Y. 1972), then District Judge Gurfein specifically warned against "Fundamental matters, largely questions of fact, . . . [being] the subject of assertion and counter-assertion without proof".

Additionally, Appellees have conceded Objectors' point that the codefendants in this case are jointly and severally

liable for the total damages the plaintiff classes have suffered. (Emhart's Br. at 15; Plaintiffs' Br. at 11) This legal principal requires that recovery from any one defendant be allocated on the same basis as the total recovery, *i.e.* on the basis of class members' purchases from *all* the defendants. Otherwise, particular plaintiff classes could well recover less than the total amount to which they are entitled.

Here, the district court has ordered that all settlement funds be placed in a *single* escrow account (A995), and simple logic dictates that the total settlement be distributed according to a single, equitable plan. Appellees have cited *no* cases where an arbitrarily allocated settlement with one or several defendants was approved, even though the total recovery by the plaintiff class would be determined at the trial of the remaining defendants. The admitted joint and several liability of the defendants is sufficient as a matter of law for rejection of the "Emhart data." If there are other settlements or judgments after the trial, all of the funds should be efficiently distributed simultaneously, but that distribution will be distorted by the Emhart plan of allocation.

In summary, Appellees have made three dispositive concessions by their admission that the plan of allocation is *necessary* to assure that the public-body class members will receive $6 million of the Emhart settlement: First, that the data presented below allegedly supporting the 80%-20% "formula" does not in fact comport with the industry's pattern of sales to public-body versus private-entity class members; second, that they led the District Court into error by urging the adoption of the unsupported 80%-20% "formula" which they now attempt to remedy by resorting to other considerations; and third, that reversal is therefore required because of the admissions that the 80%-20% plan of allocation was arbitrarily arrived at. Appellees' adamant opposition to the eminently fair claims proposal merely underscores the discriminatory treatment received by the private-entity class members.

IV. THE UNKNOWN FINANCIAL RESPONSIBILITY OF ILCO/UNICAN

Both Plaintiffs' Liaison Counsel and Ilco have diverted this Court's attention from a critical fact: the Ilco settlement is a sacrifice of nearly one million dollars which the class would have received on a transaction basis comparable to the Emhart settlement. Appellees continually assert that a fund of $85,000 is too small to be of interest, but this is true only because 90% of the classes' recovery has been surrendered.[6]

Appellees have conceded that the only support for the Ilco settlement consists of (a) the Ilco financial statements introduced into evidence by Objectors, (b) the guarded assurances of counsel who went out of their way to disclaim financial expertise, (c) the perfunctory affidavit of Ilco's Secretary—law partner of Ilco's counsel[7], and (d) a 3-page "legal memorandum" prepared by Ilco on the liability of a parent for the obligations of its subsidiaries. These submissions raise substantial and as yet unanswered questions as to the liability of Unican for the obligations of its controlled subsidiary Ilco.

As protectors of the classes' interests, Plaintiffs' Liaison Counsel should have investigated and resolved these questions before sponsoring a settlement at less than a fraction of the plaintiffs' claims against Ilco. Such a compromise is all the more suspect because the meager proceeds were designated in the proposed settlement agreement to be used exclusively to defray their counsel's own expenses. Objectors concede that the District Court took exception to this provision and indicated that it would supervise dispersal of all settlement proceeds (A995), but the settlement

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6 The dangers of evading Rule 23(e) in approving inadequate settlements are outlined in McGrough & Lerach, "Termination of Class Actions: The Judicial Role," 33 *U. Pitt. L. Rev.* 445 (1972).

7 Ilco is represented in this proceeding and generally by Bowditch & Lane. Ilco's secretary, Henry B. Dewey, is a partner in Bowditch & Lane. Furthermore, Bowditch & Lane are *Unican's counsel.*

agreement was approved by the Court with the offending clause, and it has not been deleted. Significantly, Plaintiffs' Liaison Counsel are silent on this subject in their brief.

The District Court itself was uncomfortable with the support for the Ilco settlement at the conference held in Chambers on May 21, 1976, and suggested specific remedies:

> THE COURT: So I would suppose that that application [for approval of the Ilco settlement] might also be supported by an affidavit [on] what the financial condition of the company is and the possibility or responsibility on the part of the parent company in Canada (A620-621).
>
> * * *
>
> *I don't know anything about the relationship between these companies* [Ilco and Unican] (A628-A629). (Emphasis supplied.)

The Court specifically requested certain affidavits "to satisfy the record" (A630), but they were never supplied by either Plaintiffs' Liaison Counsel or Ilco, who is uniquely in possession of the pertinent facts. Plaintiffs' Liaison Counsel now admit that a factual hearing would be necessary to decide if Ilco and Unican are truly separate entities (Plaintiffs' Br. at 43); Ilco relies on mere contentions and makes no reference to either deposition testimony or documents produced in the course of discovery to answer Objectors' admittedly legitimate questions.

The Court's perfunctory approval of the Ilco settlement likewise did not address any of the Objectors' contentions. It thus strains credulity—in light of the Court's own admission on May 21, 1976, that it know nothing of the relationship between Ilco and Unican—for Appellees to assert the Court's "familiarity with the case and all the parties" (Ilco's Br. at 7) provided the proper basis for sacrificing almost a million dollars of the classes' potential recovery from Ilco. As this Court stated in *Grinnell, supra:* "The Court must eschew any rubber stamp in favor of an independent evaluation . . ." 495 F.2d at 462.

Despite Ilco's resort to "facts" (although unsworn) outside the record which purportedly refute the inferences which Objectors have drawn from Ilco's and Unican's financial documents, the basic questions which proponents of the settlement should have resolved and which the Court below should have considered remain unanswered. For example, Unican's financial statements contain the following:[8]

> In June, 1973 [Unican] commenced construction of a new manufacturing facility in North Carolina. In May, 1974 [Unican] commenced moving inventories and equipment from its other plants [*i.e.*, Fitchburg] to North Carolina.[9]

Thus, the decision to close *Ilco* and transfer its operations to Unican's South Carolina facility was made by *Unican*, not Ilco. Likewise, the transactions which Ilco's own auditors, Peat Marwick Mitchell & Co., characterize as less than "arm's length" were undertaken by Ilco only because "the Company's parent [Unican] established certain polices with respect to transactions between the Company and its affiliate in Rocky Mount, North Carolina" (A759).

Objectors are not the first to question the distinction between Ilco and Unican. The transcript of the May 21, 1976, conference in Chambers shows that Ilco's counsel agreed to supply, in response to the doubts of Plaintiffs' Liaison Counsel and the Court, an affidavit of Mr. Fish, President of both Ilco and Unican,[10] averring that the companies are operated as separate entities (A619). None was ever supplied, although Ilco's counsel likewise repre-

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8 Unican has changed its accounting firm *four times in the past four years*, a most unusual action.

9 Notes to Consolidated Financial Statements, June 30, 1975, Unican Security Systems Ltd., p. 9.

10 It is impossible to determine if Ilco has any officers and directors independent of Unican, other than Mr. Dewey, since even such basic information as lists of corporate officials have never been provided to Objectors or the Court.

sent Unican and presumably have regular contact with its officers.

Ilco is thus forced to fall back on the wholly specious contention that Unican purchased Ilco in 1972 without expressly assuming its liabilities. Accepting this argument, Unican was free to use the profits which Ilco had illegally earned during years of violating the antitrust laws, free to transfer Ilco's profitable operations to an affiliate in North Carolina, and free to evade responsibility for any of Ilco's prior activities. As the cases which Objectors have cited make clear, the law does not permit such conduct. Furthermore, unlike the plaintiffs in *Grunin* v. *International House of Pancakes*, 513 F.2d 114 (8th Cir. 1975), *cert. denied*, 423 U.S. 864 (1975), and *In re National Student Marketing Litigation*, 68 F.R.D. 151 (D. D.C. 1974), Objectors do not seek to recover more than the defendant can afford to pay, but merely contend that the class members have a right to informed determination of Ilco/Unican's financial responsibility (A1003).

Plaintiffs' Liaison Counsel now argue that the amount of the Ilco settlement is entirely irrelevant, since "two solvent defendants remain" and "plaintiffs can recover from the non-settling defendants all of the damages caused by Ilco's conduct" (Plaintiffs' Br. at 41-42). This assumes that plaintiffs will prevail in what Plaintiffs' Liaison Counsel admit will be a "lengthy jury trial with complex issues" (Plaintiffs' Br. at 41).

Ilco and Plaintiffs' Liaison Counsel have insisted that the scant notice of the Ilco settlement which they provided to class members was sufficient, presumably since the defendant was unable to finance more complete notice. Objectors, however, believe that the notice by publication was insufficient under Rule 23(e) precisely because Ilco was settling for one-tenth of the comparable amount that Emhart had paid. Thus, even those class members who

did not object to the $7.5 million Emhart settlement might well oppose a settlement with Ilco for $85,000, especially when those proceeds were to be reserved for counsel (A875-A876).

Ilco, however, points to the "more than 20 of the 30 transcript pages" of the May 21, 1976, conference in Chambers as being devoted to resolving the problem of notice (A623-A645).[11] A review of this transcript (A615-645) reveals:

(1) Plaintiffs' Liaison Counsel proposed that *no* notice whatsoever was required (A623-A624; A631-A632).

(2) Ilco's counsel likewise suggested that no notice of the Ilco settlement need be sent, since the Emhart settlement of $7.5 million could just be inflated by Ilco's $85,000 without "any great injustice done" (A634).

(3) Ilco's counsel took the position that notice should be mailed out only *one week* prior to the fairness hearing (A635).

As the Court itself remarked, counsel were *not* concerned with "what [the notice is] going to do for the class" (A638). This cavalier approach characterized the entire course of both the Emhart and Ilco settlement proceedings.

Moreover, Plaintiffs' Liaison Counsel conveniently neglected the most obvious alternative which would have adequately notified class members but cost virtually nothing. The Emhart settlement was reached in June, *1975*, and negotiations with Ilco were conducted during February, March and April, 1976, (Ilco's Br. at 5); on March 29, 1976, the Emhart notice was mailed, obviously with counsel's full knowledge that negotiations with Ilco had been underway for more than a month. Nonetheless, after

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1 This is an exaggeration, since many of these transcript pages deal with the as yet unsolved issue of the relationship of Ilco to Unican.

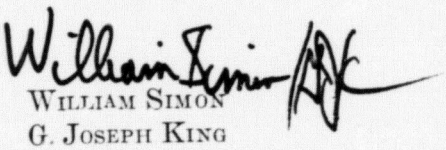
waiting more than nine months to notify the class members of the Emhart settlement, Plaintiffs' Liaison Counsel failed to protect the interests of class members by deferring the Emhart notice until the Ilco negotiations were concluded.

Owing largely to this inadequate notice, Objectors stand alone; and Ilco, Emhart and Plaintiffs' Liaison Counsel have all urged this Court to ignore the merits of Objectors' contentions. Case law, however, is clearly to the contrary, and objections should be resolved on their merits, not by counting the number of class members pressing them. In *Fricke* v. *Daylin, Inc.*, 66 F.R.D. 90 (S.D.N.Y. 1975), the District Court sustained the objections of five members of a class of 4,300 and refused to approve a settlement proposal amounting to 80% of what the plaintiffs had sought in their complaint. In *Norman* v. *McKee*, 290 F.Supp. *supra* at 32, the Court remarked that "the absence or silence of [objectors] does not relieve the judge of his duty and, in fact, adds to his responsibility" to guard the interests of the plaintiff class; the proposed settlement was disapproved. Likewise, in *Percodani* v. *Riker-Maxon Corp.*, 50 F.R.D. 473 (S.D.N.Y. 1970), the District Court disapproved a settlement as not in the best interest of the plaintiff class, even though the opinion does not reveal that any particular number of class members opposed the settlement. Obviously, the quality and character of the objections is more important than the number of objectors who come forward.

CONCLUSION

For all of the foregoing reasons, (a) the District Court's order approving the arbitrary allocation provision of the Emhart settlement agreement should be reversed and the matter remanded for the entry of an order approving the $7.5 million settlement absent any allocation provision, and (b) the District Court's order approving the Ilco settlement proposal should be reversed and the matter remanded with directions to permit discovery and hold appropriate evidentiary hearings, after proper notice to the class, on the financial responsibility of Ilco/Unican.

Respectfully submitted,



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August 30, 1976

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

IN RE MASTER KEY ANTITRUST LITIGATION EXXON CORPORATION, et al., Appellants.	Docket No. 76-7356

CERTIFICATE OF SERVICE

I, G. Joseph King, attorney for appellants in the above-entitled cause, hereby certify that on the 30th day of August, 1976, I served on appellees' counsel, Lee A. Freeman, Esquire, Freeman, Rothe, Freeman & Salzman, One IBM Plaza, Suite 3200, Chicago, Illinois, 60611; H. Laddie Montague, Jr., Esquire, David Berger P.A., 1622 Locust Street, Philadelphia, Pennsylvania, 19103; Richard M. Reynolds, Esquire, Day, Berry & Howard, One Constitution Plaza, Hartford, Connecticut, 06103; and Charles Donelan, Esquire, Bowditch & Lane, 311 Main Street, Worcester, Massachusetts, 01608, two copies of Appellants' Reply Brief, in accordance with Rule 25(a), Fed.R. App.P., in the above-referenced appeal, by depositing the same in the United States mail, first class postage prepaid.

G. Joseph King